RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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Oct. 2, 1991 **LETTER 1079**

THE MARKET: In a nutshell -- the **plus**: my Primary Trend Index keeps pushing to new highs. The **minus** -- the Transportation Average is diverging from the Dow.

THE ECONOMY: In a nutshell -- the Administration tells us the recession is over. But eight out of 10 Americans tell us we're still in recession. Who do you believe?

> Economists may say the recovery is here, but more than eight out of 10 Americans don't believe it, a new Los Angeles Times Poll shows.
>
> As the all-important Christmas shopping season nears, respondents still worry about their job prospects, and equal numbers believe that the economy could worsen or improve. Nearly one in three Americans still says the recession is serious, despite assurances to the contrary by the Bush Administration.
>
> The poll, in which 82% of respondents believe that the country was still in recession, showed little change in consumer attitudes since a Times Poll in late June.
>
> "Throughout this period of supposed recovery, the public hasn't seen it," said John Brennan, director of

From *LA Times* Sept. 26

Technically, as I've stated in recent Letters, the main problem facing this market is divergence in the Averages. The Dow has recorded a series of new highs while the Transportation Average (since June 4) has been tracing out a series of declining peaks. All this shows clearly on the page 1 chart of the Averages.

From a Dow Theory standpoint, it is important to remember that the two Averages (Industrials and Transports) must confirm each other. Movements of one Average, unconfirmed by the other, are suspect, and are more often than not -- deceptive.

What would it take to clear the air? A major technical plus would be a rally by Transports to above their last peak at **1215.44** recorded on August 23. If Transports could clear that peak, it would certainly improve the price structure from a Dow Theory standpoint.

If the market is turning seriously weak, it must show in the pattern of my Primary Trend Index (PTI). Since its January 31 "buy signal," the PTI has dipped on many occasions (always holding above its moving average), but after each dip the PTI has rallied to new highs. On September 20 (see page 2 chart), the PTI started another string of new record highs.

So that's the technical picture. What about the supply/demand equation? For one thing, we know that the institutions and funds are "cocked and loaded," ready for upside action. According to *Indata,* Pension Fund Cash recently hit an incredible low of 3.7%. Furthermore, the *Investment Co. Institute's* Mutual Fund Cash ratio has dropped to 8.6%, its lowest level in over four years. In other words, the funds and the institutions are up to their necks in stocks but very low on cash. Markets look better when the opposite is true -- when the funds and institutions are loaded with cash but very low on stocks.

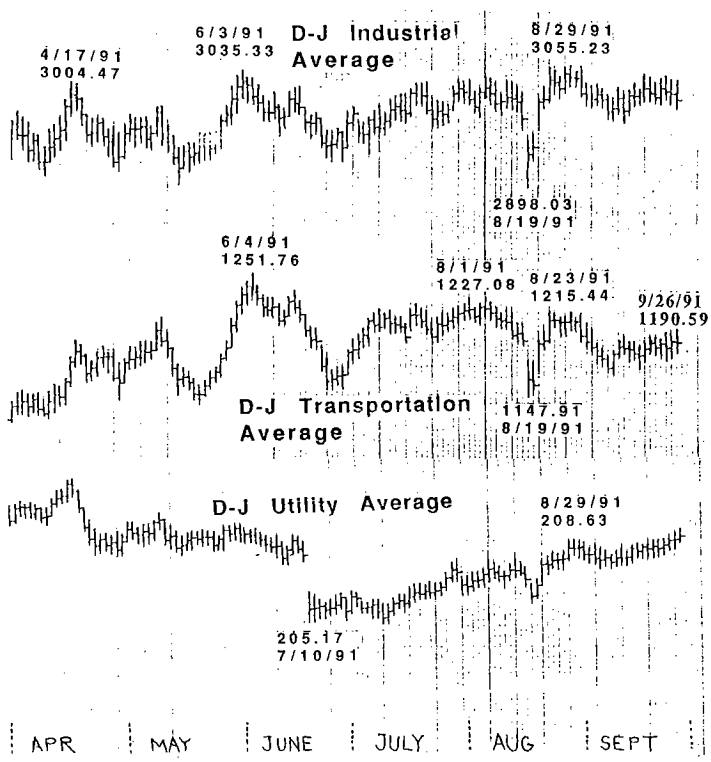
VALUATION: There's no getting around it, from a valuation standpoint, stocks are now expensive. The most reliable gauge of value is yield, the return on your investment. The latest yield figures tell us that the D-J Industrials yield 3.09% and the S&P 500 yield 3.14%.

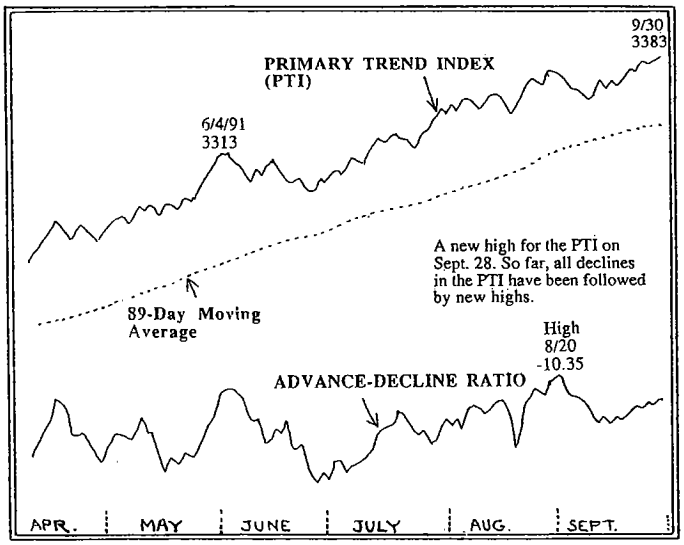
Sept. 20 DJIA 3019.23; PTI 3377; A-D Ratio -10.83
Sept. 27 DJIA 3006.04; PTI 3384; A-D Ratio -10.81
Dow Yield: 3.08%; Dow P/E: 23.0; DowPow: 50
Dow 200-day MA: 2880; Dow 30-day MA: 3005
Dow Times Book Value: 2.25; PTI 89-day MA: 3333
Percentage of Undervalued Blue-chips: 12%
Stock Summation Index: 1443 (Neutral)
Bond Summation Index: -50 (Neutral)

Is that a danger signal? Yes, but my old friend, Marty Zweig, notes that in 1972 the S&P yield dropped to a record low 2.67%, and in 1987 the yield sank to 2.69%. The S&P 500 would have to rise 16% from here if it were to equal those low yields. But Marty notes that money was tightening up in the previous instances, whereas today the Fed is actively easing. (However, Dr. Zweig doesn't mention that this is the first recession in which taxes have been raised, and that could make a difference.)

At any rate, with the Fed actively bringing down interest rates today, why couldn't the S&P rise to the point where it again yields only 2.75% or even 2.50%? And the answer is that it could. But you must realize that when you buy stocks here you are leaning against a basic principle of Dow Theory. That principle states that you buy stocks when they are great values, and you sell stocks when they are overpriced. Historically, when the Dow yield declines to 3% (which is where it is), stocks are overpriced. So from here on, it's simply a case of "how hot is hot?"

Valuation tells us where we are in the big picture. Market action tells us what stocks are actually doing, and (hopefully) what they might do in the period ahead. A basic thesis of technical analysis is -- THE MARKET IS ITS OWN BEST FORECASTER. Or as Robert Rhea, the great Dow Theorist of the 1930s put it, "The story is in the Averages."





RISK: Perhaps coincidentally, last week saw the publication of two items both dealing with that valuable but little understood subject -- risk. The first item is a new book by Justin Mamis entitled, "The Nature of Risk" (Addison-Wesley Publishing Co., $18.95). This is an excellent work by a man who has been an outstanding stock market student for decades.

The other item appeared in *Barron's* (Sept. 23). This is a must-read article entitled "Dividends Don't Lie" by Rhonda Brammer. The article describes Steve Leuthold's long-term studies of expected return, based on levels of stock yields and on levels of stock price/earnings ratios. This article is really about the risk entailed in buying stocks at different levels of dividend returns and P/E ratios.

To condense the study, Leuthold notes that the S&P 500 now yields around 3.18%. Since 1926 the S&P 500 yield has only been this low 15% of the time. These times were in late-1987, the last three-quarters of 1961 and during all of 1972. All three of these periods preceded areas of major market trouble.

Leuthold's studies entail average yields and P/Es for quarters (of a year) over a 65-year period. His historical studies show that if an investor were to buy stocks today at 3.18% yield, then looking out over a three-year span he could expect a return of only 3% annually (which is less than a T-bill would return).

Using P/E ratios instead of dividends, the statistics are even less favorable. Currently, Leuthold's "normalized" P/E ratio for the S&P 500 is 18.5. Based on this figure, Leuthold's studies show that the investor who buys stocks here and holds them for three years can expect -- a zero return, and that's with dividends included.

In other words, Leuthold's studies provide a cold look at risk and return on investment based on average statistics covering 262 quarters. Do Leuthold's statistics pin-point investment returns or guarantee that the past will replicate the future? Obviously not, since these figures deal with average risk based on past experience. Leuthold's statistics imply that if you buy stocks here, the odds indicate that three years from now you will have little or nothing to show for your investment.

Trading, buying to sell a week or six months from now, that kind of activity, has nothing to do with Leuthold's statistics. Furthermore, trading has nothing to do with long-term investment risk/reward. Buying stocks today has to do with the "greater fool" thesis. Stocks are currently in a zone which history tells us is expensive. So if you buy here, you are buying expensive stocks in the hope of selling them to someone else who will buy your stocks at an even higher price.

Will that work? It might very well work. But it goes against my personal philosophy of investing, and it goes against the odds. It also goes against my basic rule of investing which states, "Above all, don't lose money."

ECONOMICS: Do you believe all those economic statistics the US government puts out? I don't, and I never did. What do I believe? Interestingly, the September 7 London *Economist* includes a piece entitled, "The Good Statistics Guide." The *Economist* "asked a panel of statisticians from various countries to rank government statistical agencies in ten large OECD countries according to the perceived reliability of their published figures." Canada came in first, Australia second, Sweden third, Holland fourth, France fifth, Germany sixth, USA seventh, Japan eighth, Britain ninth, Italy tenth. Conclusion: US government statistics are among the least reliable of any released by the OECD nations. Incidentally, the panel stated that "integrity and objectivity" were the most important elements in the agencies releasing statistics.

I talk to a lot of people and I read a lot of newspapers and magazines. And lately, I've been getting a raft of angry mail. I can tell you this -- people out there are not happy. And the gist of it is that an economic squeeze is on.

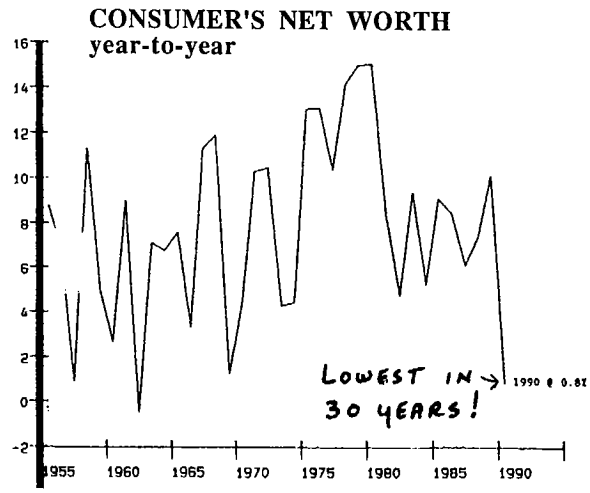
People are disgusted with all the new taxes (and the endless forms that go with them). People are up to their eyeballs in debt. People are getting hit with price rises in all directions (particularly services, licenses and medical). The value of peoples' homes has been sliding, and scariest of all, almost everyone has a neighbor or a cousin or a son or daughter who has lost his or her job and can't find another one. As one friend of mine put it -- the fundamentals of the 1991 economy are, "No jobs, no tax relief, no income growth and no confidence."

The layoffs continue, and if I had to guess I'd say that pink slips are one of the cornerstones of this recession. Within just a few days last week my local newspaper announced layoffs at Union Carbide, Frito-Lay, DuPont, NYNEX and Emerson Radio. On top of that, my favorite newspaper, the *New York Times*, just raised its newsstand price from 40 cents to 50 cents (the *LA Times* just went from 25 cents to 35 cents).

The savings rate in the US has now dropped to a minuscule 3.7%, down from a bit over 5% last May. And the economists are asking, "What's happening, why can't Americans save?" The answer, in my opinion, is taxes, rising prices, declining interest rates, and crushing levels of debt.

It's ironic, but the big decline in interest rates is actually exerting an adverse affect on most consumers. Banks and credit card issuers are reluctant to bring down their interest rates, but on the other hand consumers are finding that their CDs, T-bills, and savings accounts now produce considerably less income than before (one-sixth of all personal income now comes from interest on savings).

Economist Ed Hyman (*International Strategy and Investment*) included this chart in his Sept. 9 mailing. The chart traces



Consumer Net Worth on a year-to-year comparison. The chart shows an extraordinary plunge, a plunge taking the growth in Consumer Net Worth to its lowest level in 30 years. Hyman notes that in the latest period Consumer Net Worth (assets minus liabilities) rose only 2.3%, while consumer liabilities rose 9.4%. Now you know that can't keep up for long. The Hyman study dovetails with the figures on the current low level of Americans' savings.

Meanwhile, Mr. Bush's chief economist, Michael Boskin, announced last week (for the umpteenth time) that the recession is over, and that he expects the economy to grow between 2.5% and 3% next year. Most of the nation's economists have now fallen in line with the Boskin thesis. Well, there's safety in numbers.

So here's the big question -- is the Fed simply "pushing on a string?" And are low interest rates merely reducing consumers' income rather than jump-starting the economy? My opinion: If you're staggering under an onerous debt and tax load, if the value of your home is declining, if your company is doing badly and you're wondering whether your job is on the line, will lower interest rates tempt you to go out and buy a new Ford? Somehow, I doubt it.

RATE CUTS: The Fed has cut Fed Funds 10 times and the Discount Rate four times in an effort to beat this recession. In their latest report *Market Logic* [(800)327-6720] presents a study of instances in which the discount rate was cut four consecutive times. The study is shown below.

Market Response to 4th Consecutive Discount Rate Cut

	S&P 500 Index Percent Change		
Date of Cut	Next 3 Months	Next 6 Months	Next 12 Months
Feb. 18, 1915	+22%*	+47%*	+70%*
Sept. 22, 1922	0%*	+ 7%*	- 9%*
Mar. 14, 1930	- 5%	- 8%	-25%
Feb. 3, 1934	-11%	-23%	-22%
Apr. 18, 1958	+ 7%	+20%	+36%
Jan. 22, 1971	+ 9%	+ 4%	+ 8%
Mar. 7, 1975	+ 8%	0%	+19%
July 30, 1982	+13%	+21%	+35%
Mar. 7, 1986	+ 6%	+10%	+28%
Median	+ 7%	+ 7%	+19%

(*DJIA)

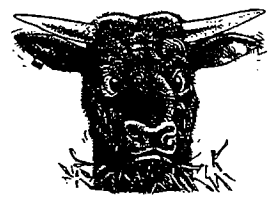
Market Logic also reminds us of two well-known Wall Street adages, "Never fight the Fed," and "Never fight the tape." Now I'll let you in on a third one -- "Never fight the primary trend of the market."

Referring to the statistics, we should note that there were three instances when the S&P 500 was down a year after the Fed had cut the Discount Rate four times in a row. How could that be? The difference was whether stocks were in a bull or bear market. In 1922 the market was in the grip of a mini-bear market that lasted until 1923. In 1930 the market was in the grip of the worst bear market in history. In 1934 the market had just bounced mightily off the horrendous 1932 bottom, and stocks in 1934 were correcting (downward) following the bounce.

In two of the three instances, the primary trend was bearish. In the third instance -- 1934 -- the market was in an extraordinary correction.

So let me put it this way. If the primary trend of the market (today) is still bullish, then in due time those four Discount Rate cuts will almost surely work as a plus for both the market and the economy. BUT -- if the primary trend is now in the process of turning bearish, the Discount Rate cuts will be washed away like so much chaff in the wind.

INVESTMENT POSITION: The bull is in the box. He's mumbling to himself, "Don't fight the Fed, don't fight the tape, don't fight the PTI." But he's reading the latest auto and home sales figures (he probably shouldn't do that) and he's got an upset stomach.



What am I doing? I'm just sitting tight. From a risk/reward standpoint, I don't see anything brilliant to do at this time. Sure, I can pick out strong stocks (JP Morgan, Amer. Home Products, Harley Davidson), but I'm still going to sit tight. This market's expensive, and I've got loads of patience.

I get the feeling that the only people having "fun" here are the program traders. They're jazzing stocks up one day, dumping them the next. If you're at a loss for what to do and you've got money to spend, tell your broker to buy you some T-bills. Relax, take it easy. The NYSE will be here a year from now and 50 years from now. My guess is that there will be all sorts of intelligent things to do before long -- trust me.

PARABOLA: If one picture is worth 1,000 words, the picture on page 4 may be worth a book or two. This startling chart was just sent to me by my computer genius friend, John Carder. John has his own computer/chart firm, and when something interesting comes along or when he discovers something, he usually sends it to me.

Here's what John writes to accompany the chart. "This chart is visually arresting. You'll note that the chart is drawn on a log scale. That means that the slope (steepness) of the parabola is proportional to a compound rate of growth. These are true parabolas, so the slope increases linearly with time.

"I haven't worked with these parabolas long enough to know if they're predictive. The reason I'm FAXing you the chart is that it characterizes my feel for the market. Since the December 1974 bottom, we've experienced an explosive rise in stock prices. Following the 1987 crash, stocks were struggling to stay above that lower parabola. Last year's correction was a clear break. This year's advance on Desert Storm euphoria has not been able to regain that lost momentum.

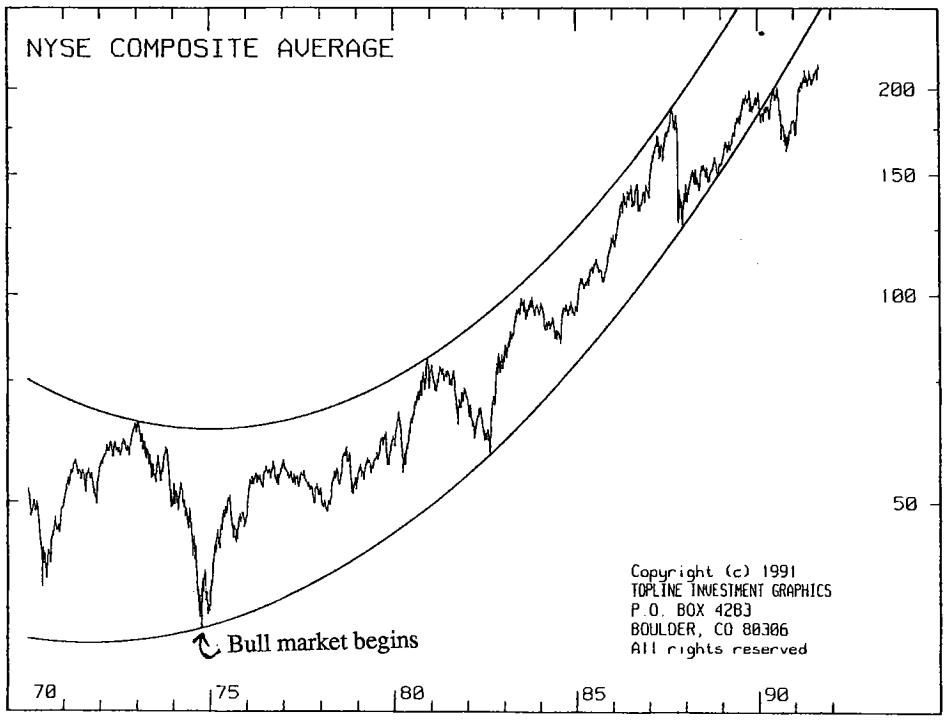
"As I said, I don't know how predictive these things will turn out to be, but it isn't a pretty picture."

Russell comment: My own experience with parabolas is that all break down at some point (obviously). Following a parabola break, there is often a second weaker upward thrust as the price movement seeks to regain its lost upward momentum -- and the failed second upward thrust is then followed by a vicious bear market.

I was particularly interested to see that John measures the whole parabolic rise from the 1974 low (577 on the Dow). That's the point at which I have always maintained that the great bull market started -- not 1982, not 1984, but 1974.

I do think that what this chart shows is the major break in the upward momentum of the market. Since the 1989 decline, the NYSE Composite has clearly been trying to regain its upward momentum, but so far it has not been able to climb back into the area of the lower parabola. Since the pattern of the parabolas continues to rise and since the NYSE Composite has been going sideways for many months, we can see that the chance of the Composite rallying back into the parabolic pattern is about zero.

What happens next? It will be fascinating to find out, but a bull market may be likened to a ball that is tossed up in the air. At some point in the ascent, momentum halts and the ball hangs suspended motionless in the air for a moment. Then momentum begins its descent and momentum starts to build to the downside as the ball returns to earth. Is the stock market now at the motionless point in



the upward momentum cycle? Time will tell. But as I said, it is a fascinating picture.

NOTES & QUOTES: Last week I heard a labor leader on CNN say, "Fear of the Red Menace has changed to fear of the pink slip." Sounds right to me.

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An Office of Management and Budget forecast for the five-year cumulative federal deficit has changed. From the original estimate of $62.3 billion, the forecast has zoomed to $1.087 trillion (that's right, trillion). The *National Review* called Budget Director Darman's performance "the most disastrous failure in the history of the job."

* *

I said it from the beginning, and I've been saying it ever since. The decision to go to war, then abruptly pull out while leaving Saddam Hussein still in power, was one of the stupidest miscalculations any US President has ever made. Meanwhile, Saddam has been rebuilding his military and power base while playing cat-and-mouse with the US and the UN forces. Finally, as the situation reached the intolerable stage, Bush has threatened to use force again. Even the *Wall Street Journal*, an ardent Bush supporter, said in its Sept. 19 editorial, "We hope Mr. Bush's Wednesday actions are more than just a bluff. Mr. Bush's vision of a stable Middle East cannot possibly be fulfilled while the Iraqi dictator remains in power. It's time to finish the war and secure the peace."

Russell comment: Saddam is obviously using every trick in the book to frustrate the allies and to show the Arab world that it was he that won the war against "the American bullies." Bush no-win dilemma: He must lose face by going to war again, or he must lose face by backing down while Saddam does his dance of deception. What about all those victory parades? Don't ask.

* *

By the way, the US' bill for Desert Storm was $60 billion (although with new military movements it will continue to build). So far, we've been paid $42 billion by our allies. The two nations that benefited the most, Kuwait and Saudi Arabia, have not yet paid in full.

* *

I had breakfast last week with a good friend who is a nuclear physicist with a San Diego defense firm. I asked him what the effect would be in his industry as the huge defense establishment shrinks, as it inevitably will. He answered, "The effect will be disastrous from an employment standpoint, particularly in Southern California. But the worst part is this -- all these scientists and researchers who are employed by defense companies will have no place to go. Almost all the new research and development, almost all the new processes and concepts, have come as a direct or indirect result of defense research. The US is falling behind now in valuable research and development, but as the defense establishment contracts, it's going to play havoc with this country's future. I'm very depressed about the whole picture."

* *

Unfavorable tax laws in the US are discouraging venture capital. It discourages capital to the point where many new companies are now seeking out foreign investors (particularly the Japanese) to finance their ventures. Said Ian Ross, former president of AT&T Bell Laboratories, "What I think is happening in the final analysis is that the benefits of technology . . . developed with the ingenuity of our private enterprise . . . are shifting to the Japanese. I don't blame them for that. It's our fault, not their fault." Note: during 1987-90 the Japanese invested $4.9 billion in US computer and related industries alone. During the same period, France invested over $2 billion.

* *

France Says Japan Plans To Control Car Market

Compiled by Our Staff From Dispatches

PARIS — Japanese automakers are planning to "swallow up" their European rivals as soon as the European market is fully opened to them in the year 2000, the French foreign trade and industry minister, Dominique Strauss-Kahn, said Wednesday.

"The presidents of the Japanese automobile groups are saying 'our aim is not to make the European car disappear,'" Mr. Strauss-Kahn said in an interview with the newspaper Le Figaro.

Last week it was announced that the US trade deficit surged to $5.9 billion. Earlier in the week the (almost embarrassed) Japanese announced that their total trade surplus was up a whopping 70% in August. So the Japanese industrial juggernaut rolls on, scaring the devil out of US and European authorities.

During the same week French authorities stated that Japanese auto makers are planning to "swallow up" their European rivals as soon as the European market is fully opened to them in the year 2000. If you've ever driven a Lexus or an Infiniti you can believe it. Here's a headline from the *International Herald Tribune* (which happens to be one of my favorite papers).

* *

German miracle? This surprising story from the Sept. 14 *Economist:* "The mood is shifting. Visibly, eastern Germany is being transformed: new roads, new factories, new shops. Until recently no east German bought an east-German product willingly. It was a matter of pride. Regardless of price, things had to come from the west. Now the distinction is ceasing to matter. More east-German goods are being made and marked to western standards. Before long nobody will care what comes from where. In that sense economic integration is already a fact . . . On September 9th Helmut Kohl told a meeting of unions and employers that less than a year after the eastern Landers were fully absorbed into the federal republic, the recovery was underway . . . Private as well as public investment is pouring in. Construction is booming. After a slow start, the Treuhandanstalt is privatizing 100 enterprises a week. Euphoria is just around the corner."

* *

In the Sept. 15 *Washington Post National Weekly*, economist Robert Samuelson writes, "You have to grasp the enormousness of the impending Soviet economic failure. In the Great Depression, US gross national product dropped 30% between 1929 and 1933. It didn't regain its 1929 level again until 1939. Unemployment averaged 18% for the decade. The Soviet Union is now

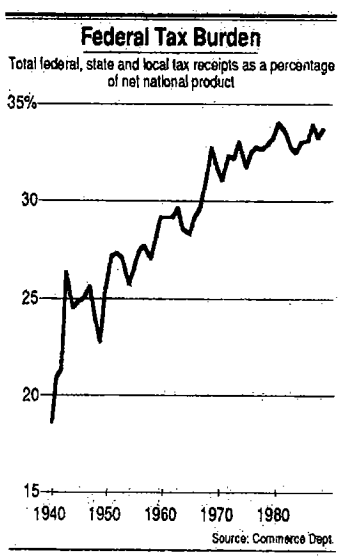
approaching a comparable calamity. In the first half of 1991 its GNP declined about 10%. By the end of 1991 it's going to fall 20%."

* *

California: I've been writing about California's hostile atmosphere towards business. It continues. *California Business Roundup* conducted a survey which shows that 41% of companies in the state have plans to expand outside of California and 14% of the companies intend to relocate outside the state.

* *

The complaints about rising taxes have grown to a roar. This chart, courtesy *Investor's Business Daily,* shows what has been happening. There has been a steady rise in total tax take on the part of the cities, the states and the federal government. Currently, the total take is now approximately 33% of the entire net national product.



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I've been writing about subscribers who have escaped taxes and other nasty items -- and I've been getting lots of replies. This is from a subscriber in the Canary Islands off the coast of Spain. "You can't beat the Canary Islands. I built a 4,500 ft. mansion in 1981 for $320,000. Today it's worth $2 million. Annual property taxes (one acre walled garden) is $458. My diesel car license costs $53 a year. Hawaii has nothing compared to the beauty of the Canary Islands, where we have eternal spring climate and the best flight connections to anywhere." (H.C., Gran Canaria, Spain). Russell comment: It sounds great. In fact, it sounds like La Jolla without the people, the traffic and the taxes.

* *

The Sept. 20 *WSJ* ran a global ranking of risk, based on political, financial and economic risks for 129 nations. Safest all around nations were: #1 Switzerland, #2 Luxembourg, #3 Norway, #4 Austria, #5 Germany, #6 Netherlands, #7 Brunei, #8 Japan, #9 Singapore, #10 USA, #11 Canada. Bottom of the list included Cuba, Bangladesh, Lebanon, Sierra Leone, Zaire, Haiti, Ethiopia, Uganda, Burma, Iraq, Sudan, Somalia, Liberia. There, now you know where to live and where not to live.

* *

Speaking of the military, everyone seems to be waiting for the big "peace dividend." I'll repeat, there isn't going to be any peace dividend. First, the military will resist mightily any move to cut its actual (nominal) budget. Second, if there are any savings they'll be spent before they arrive. The great cartoonist, Wasserman, presents here what is probably the Pentagon attitude.

FINALLY! A PEACE DIVIDEND!
NOPE— WE NEED MORE MONEY FOR THE MILITARY
MORE?! BUT THE SOVIET UNION IS SPLINTERING INTO 15 PIECES
THAT'S 14 MORE POTENTIAL ENEMIES THAN BEFORE!

BERLIN — You can order one, but it may take six months to get here. You can rent one, but book way ahead. You can buy an old one, but it may cost as much as a new one.

Europe has gone a little hog wild over Harley-Davidson, the quintessential American motorcycle, the classic "Hog" with the Big Bob tank.

The Milwaukee-based manufacturer is a bit baffled by the sudden fascination among foreigners with the big, bad bike.

"We are totally hot right now. It's really amazing," said Catherine Tenke of Harley's international marketing department.

In 1988, the company peddled 9,400 Harleys overseas, about 16 percent of its total $400 million in sales. Last year, it sold 16,000, nearly 30 percent of its $600 million in sales, she said.

This year, the company expects to sell about 20,000 bikes in its main export markets: Britain, France, Australia, Japan and the largest foreign customer, Germany.

Boom: Open any magazine today, and you'll see a picture of a macho guy, some Hollywood hero or some luscious damsel perched atop a Harley Davidson motorcyle. Motorcyles are "in," motorcycle jackets are all the rage. Meanwhile, Harley stock keeps going up and up. Harley is the hottest motor company on the planet, and in the last year its stock has boomed from 13 3/8 to a current 57. Harley still can't deliver their bikes, and now Europe and Japan are wild for them. You heard it here first -- over a year ago.

* *

Armani, the man who made the $2,000 power suit a "must" for the upwardly-mobile man, is saying that T-shirts and blue jeans will be "the staples for the '90s." Says Armani, "I think consumerism has been taken to the limits. People are tired of being bombarded by all the new names in fashion." Armani plans to open a moderately-priced chain of retail stores in the US featuring jeans, T-shirts and casual clothes. Don't laugh at Armani. His total revenue last year was over half a billion dollars, so he knows what he's talking about.

* *

Want to cash in on the new Soviets? The Overseas Private Investment Corp. (OPIC), a US government agency, will help. OPIC plans to offer up to $1 billion (10% of OPIC's global portfolio) in loans and guarantees to US investors who want to do business with the Soviets. The big problem now for the Soviets -- to get through a Russian winter while avoiding starvation.

* *

Does music reflect the tenor of the times? I think it does. I grew up with the excitement of swing, and the romance of ballads. In those days the words to the song plus the music itself was more important than who played or sung. That was the 1940s. In those days pop music was played by adult musicians. In the late '50s the kids started to play their own music. "Healthy" rock was in. The '60s saw acid rock, the rise of kid-power, Woodstock, protest music and dope. The '70s saw more of the same although the rock got harder and the dope got stronger. The '80s saw the rise of heavy metal, many foreign bands, wild antics on stage, and towards the end of the '80s -- rap. Turn on MTV today and what you get is far more visual than musical. Basically it's sex and violence. Some of the "acts" on MTV are so openly violent and sexual that I find myself mumbling, "No wonder so many kids today have grown immune to violence and sex. Sado-masochism and violence is flooding the TV channels." Question: do TV and the movies merely reflect life -- or does what people see on TV and in the movies impact on their thoughts and actions? Answer: I think both are true. Comment: A few years ago when "Married With Children" first hit the Fox channel, advertisers pulled out, complaining that it was obscene. The public loved it. Now "Married" is on five days a week and nobody thinks twice about it.

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I spent the first 35 years of my life in Manhattan, so naturally I still have an intense interest in Gotham. New York isn't the same city that I left in 1961. In those days I could walk through Central Park at midnight without fear of getting killed, I could take the subway from one end of the city to the other without being mugged, I could stroll down Broadway from 96th Street to Times Square without stumbling over garbage or vagrants sleeping in doorways.

So I was interested to read Mayor Dinkin's just issued report on the city. Here's how the *NY Times* described it: "The Mayor's Management Report, an annual survey that has been issued since the fiscal crisis of the mid-1970s, found dirtier streets, more homeless families in temporary housing and more children in foster care, spiraling demand for social services for AIDS cases, a drop in

the portion of the city's garbage that is recycled and a swelling jail population . . . The growing welfare rolls, amounting to about one-eighth of the city's population, accelerates a trend that began in 1990. On June 30 the city had about 937,000 people on the welfare rolls, up from 860,000 the year before." Russell comment: This disastrous report is in line with what's happening in many large US cities. Where it all ends I don't know.

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Do you know about the House bank, the private bank run for the benefit of members of the House of Representatives? This bank never calls a member for a bounced check, it simply covers for them. During the first six months of 1990 House members wrote an incredible 4004 bum checks with insufficient funds (19 bad checks per representative). But the House bank covered them all. And these are the rubber-check writers who are supposed to manage the nation's money. Once more I say, LIMITED TERMS for Congress. If we're not smart enough to vote 'em out, let's put an "automatic jettison" law on the books. Flash: Rep. Foley just announced that he's ending the nonsense at the House bank.

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Did you see *Forbes'* list of top income for entertainers? Gad, the five "New Kids On the Block" (rockers) made $115 million during 1990 and 1991. For the same two year period Bill Cosby made $113 million, Oprah Winfrey made $80 million, Madonna made $63 million, Michael Jackson made $60 million, Kevin Costner made $59 million, Johnny Carson made $55 million, the Rolling Stones made $55 million, Eddie Murphy made $42 million, Arnold (Schwarzenegger, that is) made $35 million, Aerosmith made $34 million, Jack Nicholson made $30 million, Michael Douglas made $27 million, Michael J. Fox made $26 million, Guns 'N Roses made $25 million. Even Vanilla Ice made $18 million. And Frankie (Blue Eyes) made $27 million. The other side of the coin is that at any given time, 90% of Actor's Equity is on unemployment, so I guess it ain't that easy.

GOLD and the DOLLAR: The big debate in the Soviets is whether to stay with one currency or to allow each of the Soviet nations to issue their own currency. Sensibly, there should be a single, convertible currency. Georgy Matyukhin, chairman of Russia's central bank, states, "It will take two years for the ruble to catch on." My question -- catch on to what? They have to give the ruble credibility, and I don't know how they can do it without a gold backing. Matyukhin has stated that Russia hasn't got enough gold to back the ruble successfully.

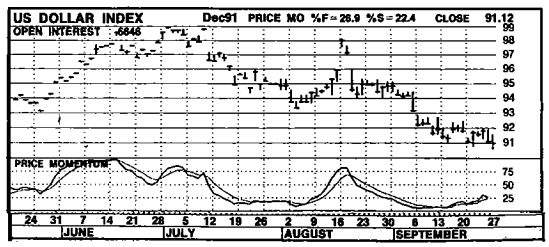
SHOCKER -- Matyukhin knows what he's talking about. On Sept. 28 the *LA Times* headlined the story that the Soviets, incredibly, have sold off two-thirds of their gold reserves! They now have only 240 tons of gold worth about $2.7 billion. "The huge gold sales," runs the article, "even more extensive than most Western estimates, underscored the disintegration of the Soviet economy. 'Where did it all go?' asked Mikhail Berger, the economics commentator at the newspaper *Izvestia*, 'How did we manage to squander so much money so quickly? At this rate, we will not have an ounce of gold in 12 months time.' In the last three months alone, Moscow appears to have sold about 134 tons of gold -- about $1.5 billion worth -- to pay debts due foreign companies . . . the Soviet Union spent all of its $15 billion in foreign currency reserves last year, Yavlinsky said, and the government is about $4 billion overdrawn at its foreign banks." Russell translation -- The Soviet Union is bankrupt, and I mean BROKE.

As to the future of the ruble, who knows? Inflation is now sweeping Russia, and the ruble is so discredited that an increasing amount of trade is via barter, even at the business level.

What I can't understand is why these numbskulls didn't back the ruble with gold while they had the chance -- or at least use their gold as collateral for loans or for backing bonds. Of course, if the Soviets ever had the brains to back the ruble with gold, the US would probably complain bitterly. Why? A gold-backed currency would be a threat to the dollar, which is backed by nothing except the US' proclamation that the dollar is "legal tender" for all debts. Let's face it -- Washington wants the world to trust its politicians, not gold.

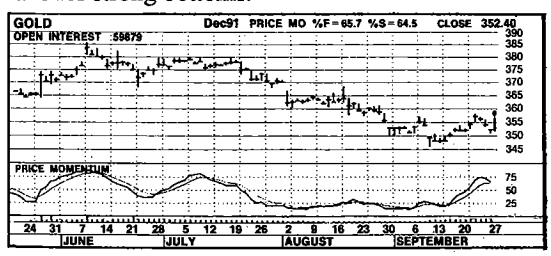
Meanwhile, despite gaping federal deficits, there remains an incredible amount of confidence in the dollar. Also, the dollar is still "cheap" on a purchasing power parity basis (in other words, the dollar buys a lot in the US compared with what a comparable amount of French francs would buy in France).

Ultimately, however, currencies move on the basis of supply and demand. And if nothing else, a sick economy and steadily declining interest rates in the US make the dollar less attractive to foreign investors. Furthermore, the unending string of US federal budget deficits tells investors that the dollar is anything but a long-term holding or a store of value. On Sept. 30 the Dollar Index (Dec. contract) broke to a new low below 92. This chart from *Investor's Business Daily* shows the latest swoon in the dollar (which is now oversold and has been "trying" to base).



On the news of the Soviet "no-gold" situation, gold jumped early this week to above 354 (spot) level. The 40-day moving average for gold (basis the December contract) is 357. On Monday, Sept. 30, gold rallied to as high as 359.50, well above its 40-day moving average. It will be a major technical plus if December gold can hold above 357.

The commercials (big commercial users) are still heavily on the buy side of gold while the smaller speculators are heavily short. The sentiment towards gold remains vehemently bearish (even the gold advisories are on the sidelines). This is the type of sentiment that can make for strong bottoms.



LATE NOTES: The stock market continues to be engaged in what I term high-level "churning." The blue-chip investment-grade issues have stalled out, and buying is centered in the medium to smaller stocks with an emphasis on bio-tech issues.

However, two warning signals have surfaced. The first is a warning from the Arms Index (TRIN) -- see the article in *Barron's*, Sept. 30, page 17. The second warning comes from my friend, David Fuller, out of London by FAX (David publishes international chart books plus the international *Fuller Money* report). David's message reads as follows: "My Chart Analysis World Market Indicator gave a global sell signal on Monday (Sept. 23) only the fourth sell signal in the last eight years."

The realization is slowly emerging that this recession is considerably worse than what Washington would have us believe. That realization also leads to the feeling that the Fed must lower interest rates even further. The stock market has been trading off the declining interest rates, but there is a limit to such action. Somewhere along the line the economy must go up -- or the stock market will go down.

I'll say it again -- the critical item here is whether the primary trend is bullish or bearish. If the primary trend remains bullish, then lower interest rates will ultimately do the trick. But if the primary trend is in the process of turning bearish then the Fed can give money away, and business (and ultimately the market) will continue to deteriorate.

NEXT MAILING: Oct. 16